

CLEVELAND PUBLIC LIBRARY
BUSINESS INF. BUR.
CORPORATION FILE

S.S. Kresge
Company
Annual Report
1971

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Annual Meeting

The Annual Meeting will be held the third Wednesday of June (June 21, 1972) at 10 a.m. at the Masonic Temple, 500 Temple Avenue, Detroit, Michigan.

Transfer Agents

National Bank of Detroit, Detroit, Michigan
The Chase Manhattan Bank N.A., New York, New York
United California Bank, Los Angeles, California

Registrars

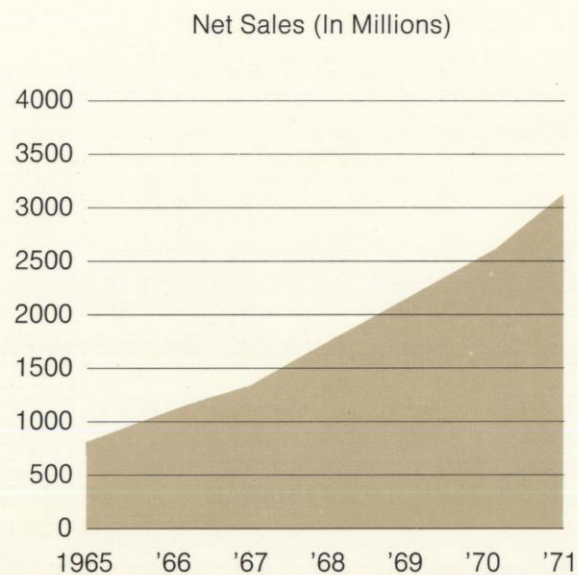
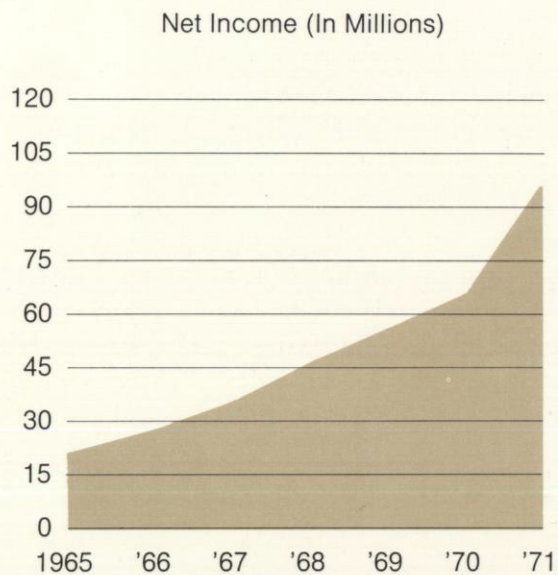
Manufacturers National Bank of Detroit, Detroit, Michigan
First National City Bank, New York, New York
Bank of America, Los Angeles, California

Trustee

5% Convertible Subordinated Debentures
National Bank of Detroit, Detroit, Michigan

1971 Highlights

	1971	1970
Sales	\$3,100,216,000	\$2,558,712,000
K mart, Kresge and Jupiter stores	1,122	1,073
Net income	\$ 96,116,000	\$ 66,994,000
Earnings per common and common equivalent share	\$2.56	\$1.86
Cash dividends declared Per share	\$ 18,233,000 50¢	\$ 15,938,000 44¢
Employee compensation and benefits Per sales dollar	\$ 448,876,000 14.48%	\$ 375,713,000 14.68%
Depreciation and amortization Per sales dollar	\$ 27,642,000 .89%	\$ 23,737,000 .93%
Fixed asset additions	\$ 82,539,000	\$ 58,720,000



To Our Shareholders

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Record increases in consolidated sales and profits for the 52 weeks ended January 26, 1972 were due to continued improvement in operating results of Kresge's K mart stores and substantial progress by all subsidiary operations.

Our sales gain reflected the contribution of new stores and further growth of K mart's acceptance by value-conscious customers of all income groups.

The significant profit-margin improvement was produced by more efficient merchandise procurement and strengthened control of operating costs and inventory shortages. Increased sales were also importantly helpful in reducing overhead and expansion expense ratios.

Price controls applied primarily to the important last four months of the year. Since few regular sales prices are usually increased during this period, our announced policy of increasing no regular sales prices from August 15 to February 1, regardless of cost increases, had minimal effect on profits.

Seventy-four K marts and one new Kresge variety store were opened last year. We also reopened one K mart and one Jupiter store that had been destroyed by fire in 1970. Major refurbishings were completed at 36 locations, and one Kresge store was converted to the Jupiter discount operation.

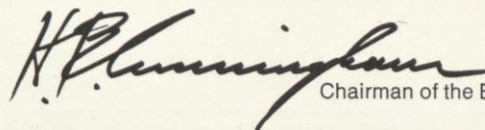
Twenty-seven unprofitable Kresge and Jupiter stores were closed during the year.

Prospects for the current fiscal year are generally encouraging. While present sales comparisons are slightly less favorable than increases enjoyed in early 1971—partially due to decreases in the variety-store division—operating margins continue at a healthy level. Our building program will be at least as extensive as last year's, and the steady growth of K mart's market share is expected to be sustained.

Logical questions may be raised regarding Kresge's capability to maintain a comparable future growth pattern. It obviously becomes more difficult to show extraordinary percentage gains as the volume base enlarges. However, the expansion rate of our new-store construction schedule is projected to increase gradually, and no profit deterioration is anticipated except as may be warranted by market conditions or government controls.

In many respects, our 1971 showing represents a culmination of efforts to implement concepts developed during the 10 years since the first K mart store opened on March 1, 1962. And the decade ahead is contemplated with the assurance of a strengthened organization of experienced and dedicated Kresge people well prepared at all levels to meet future challenges.

March 6, 1972


Chairman of the Board



They were people who weren't supposed to know how. People like a Kresge hardware buyer, a Kresge ready-to-wear buyer, a K mart sales promotion manager. The Kresge Company charged them with the responsibility of establishing a subsidiary to merchandise and operate sporting goods and automotive accessories and service departments in American K mart discount department stores. Business and industry observers sat back and waited.

The Start of Success . . . Sporting goods for 380 K marts came via 87 rail cars, 137 piggybacks and 2,600 trucks to a K mart Enterprises, Inc. distribution center in Royal Oak, Michigan, last year. KEI is the Kresge Company subsidiary that merchandises and operates sporting goods and automotive accessories and service departments in American K marts.

Some six years later, the subsidiary's president, E. James Haglund (the former hardware buyer), and his staff look with justifiable satisfaction upon their creation—K mart Enterprises, Inc. The parent company's sporting goods and automotive subsidiary showed a 42 percent increase in sales in 1971. Operating profits also increased significantly.

KEI had its modest beginning in December 1965 when the Kresge Company acquired a licensee which had been operating 42 sporting goods departments in K marts. The subsidiary's home office staff of 29 was then directing these 42 departments in 11 states.

The subsidiary assumed the management of other sporting goods departments operated by the parent company as well as those opening in all new K marts. On December 31, 1966, the young firm was operating 134 departments. To accommodate this spectacular growth, a modern 133,220-square-foot administrative office and warehouse was purchased

in Royal Oak, Michigan. The new company had accomplished its first goal—making K mart sporting goods departments more profitable, more efficient and customer oriented.

Now KEI was ready for its second challenge—operating automotive accessories and service departments. The decision was made that all automotive centers opened after February 1, 1969 would be KEI operations. The first departments made their debuts that February in two California cities. At the close of 1969 the subsidiary operated automotive centers in the 53 K marts opened that year throughout the United States plus three centers formerly operated by a licensee. In January 1972, KEI had 189 auto



departments in 41 states.

Auto centers are being operated by a licensee in 233 other stores due to an agreement made before KEI was founded. These units will come under KEI's control in less than four years. By 1975, with present K mart expansion plans, KEI will be operating over 650 automotive departments.

A home office and warehouse staff of over 250 people now directs the automotive centers and more than 420 sporting goods departments. With approximately 5,000 employees in stores from coast-to-coast, and an anticipated manpower need of about 9,000 by 1975, KEI's top management utilizes a field network as liaison between store personnel and the Royal Oak headquarters.

There are sporting goods regional offices in Los Angeles, Houston, Royal Oak,

K mart contributes importantly to the growing popularity of tennis and games by offering the broadest assortment of competitively-priced merchandise in the country.

Atlanta, Youngstown and Chicago. Automotive regional offices are located in Los Angeles, Atlanta and Royal Oak. Regional managers and assistant regional managers work closely with district managers in implementing home office policies on merchandising, operation, display and customer service at store level.

The sporting goods and automotive divisions have personnel directors at KEI headquarters who, with district managers, are responsible for recruiting management trainees. These young people are required to take four to six months of intensive in-store training before appointment to managerial posts.

As in the parent company, promotion from within is KEI's policy. District managers, regional officers and many home office executives have progressed from store management positions.

Although K marts are basically self-service stores, the nature of sporting goods and automotive equipment requires the availability of knowledgeable

sales people and personal service.

Every sporting goods department, comprising approximately 3,000 square feet, has qualified employees, including a manager and an assistant manager, to advise customers.

KEI officials emphasize that "we sell service" in our automotive centers. Staffs large enough to give needed customer assistance are always on duty in these

departments which comprise about 5,000 square feet including the service areas. Approximately 60 percent of sales is derived from auto accessories and 20 percent from tires. Since the remaining 20 percent of automotive volume is generated by service areas, it is essential that qualified mechanics be on duty at all times. New service areas become profitable only when customers become convinced that capable help is available to handle their automotive needs. That KEI's store staffs have established this customer



KEI's Royal Oak distribution center can fill orders daily for more than 65 K marts. In 1971, the center shipped 12 million pounds of merchandise to K marts.



Fishing equipment produces 25 percent of the average K mart's sporting goods volume.



KEI purchases merchandise from 550 suppliers in the United States, Canada, the Orient and Europe.



K mart has hit a hole-in-one with its complete line of golf equipment featuring famous name brands.



K mart sporting goods departments are merchandised individually so that assortments can be tailored to geographic locations and local preferences.

confidence is evidenced by the fact that most service departments show more than a 10 percent increase in volume each year. Anything sold in the accessories department can be installed by K mart mechanics.

These are the people of KEI—ready to serve sports enthusiasts and car owners with assortments of merchandise that are as complete as can be found in competitive retailers and in most specialty shops.

K mart sporting goods departments offer complete lines of sporting equipment for each season. Stores are merchandised individually so that assortments can be tailored to geographic locations and



The success of K mart sporting goods and automotive departments is vitally tied to this Kresge philosophy.

local preferences.

A general list of sporting items featured in season includes fishing, baseball, football, golf, tennis, skiing, bowling, basketball, archery and hunting equipment; outdoor and indoor games such as badminton and volley ball; camping and exercise equipment; clothing for all sports and hunting and fishing licenses.

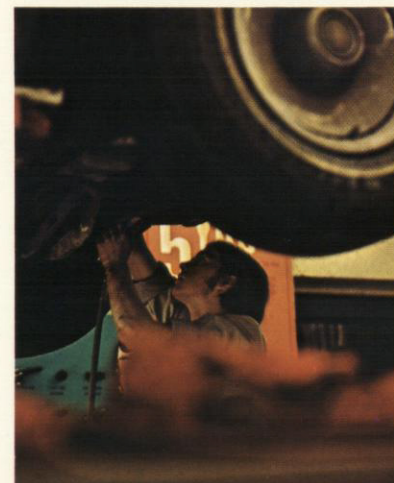
Shoppers in K mart automotive departments will find full lines of K mart private brand tires, batteries and accessories—all laboratory tested for quality control—and a wide assortment of popular nationally-advertised products. It is especially noteworthy that K mart's private label auto goods generally outsells national brands.

Outstanding features of the departments are sound centers offering a wide selection of stereo tape players and tapes. These centers are among the most complete in the United States.

The service areas have six to nine bays to expedite light maintenance and replacement work such as tire installations, checking and replacement of brakes, tail pipes and mufflers, and wheel alignments and balancing.

To those business and industry observers who sat back and waited, K mart

Enterprises, Inc. proudly reports that not only are its automotive and sporting goods departments profitable but most are in the black within a short period after opening. KEI's home office staff, field personnel, store managers and employees are obviously people who know how to accomplish their mission.



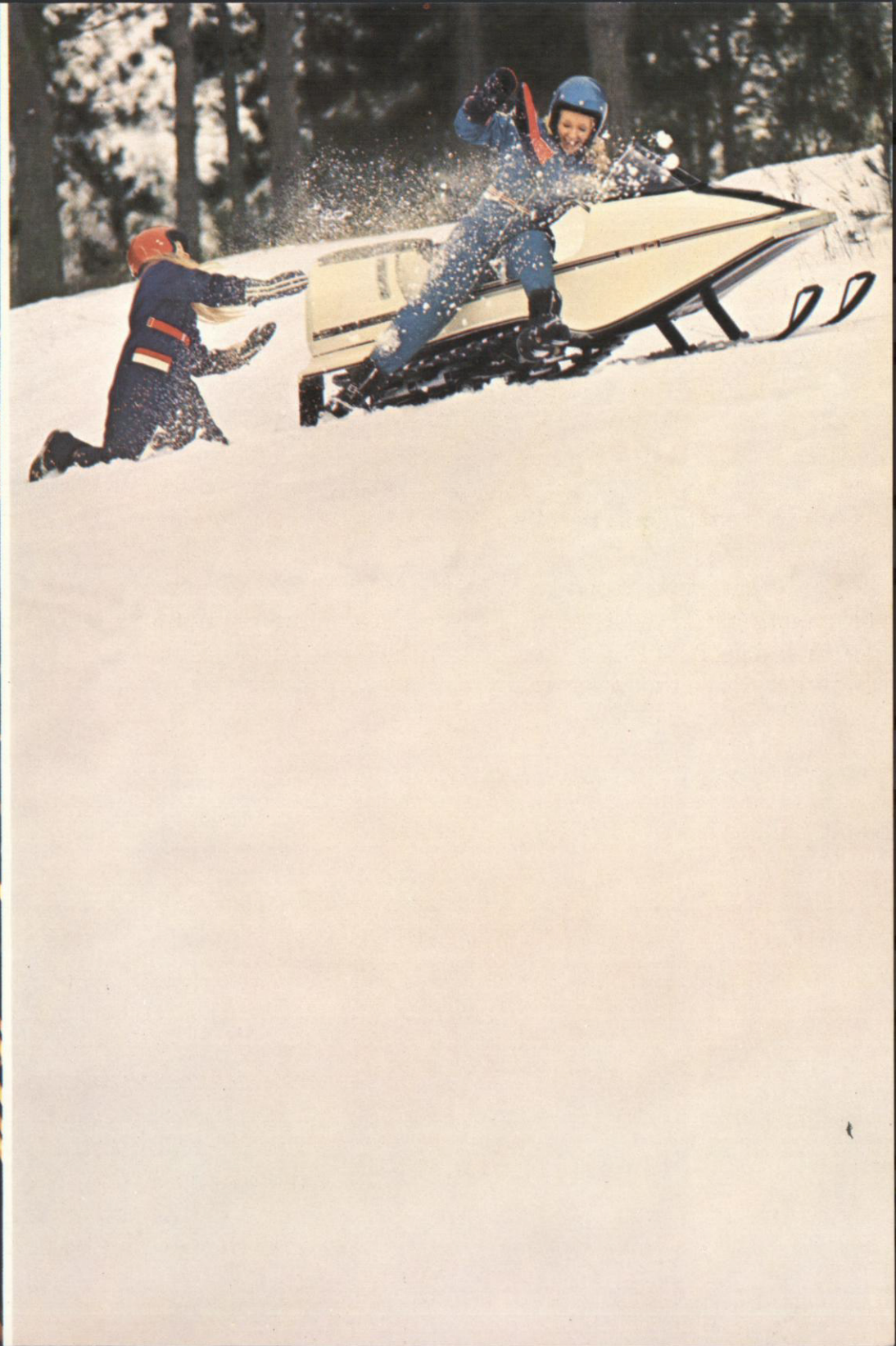
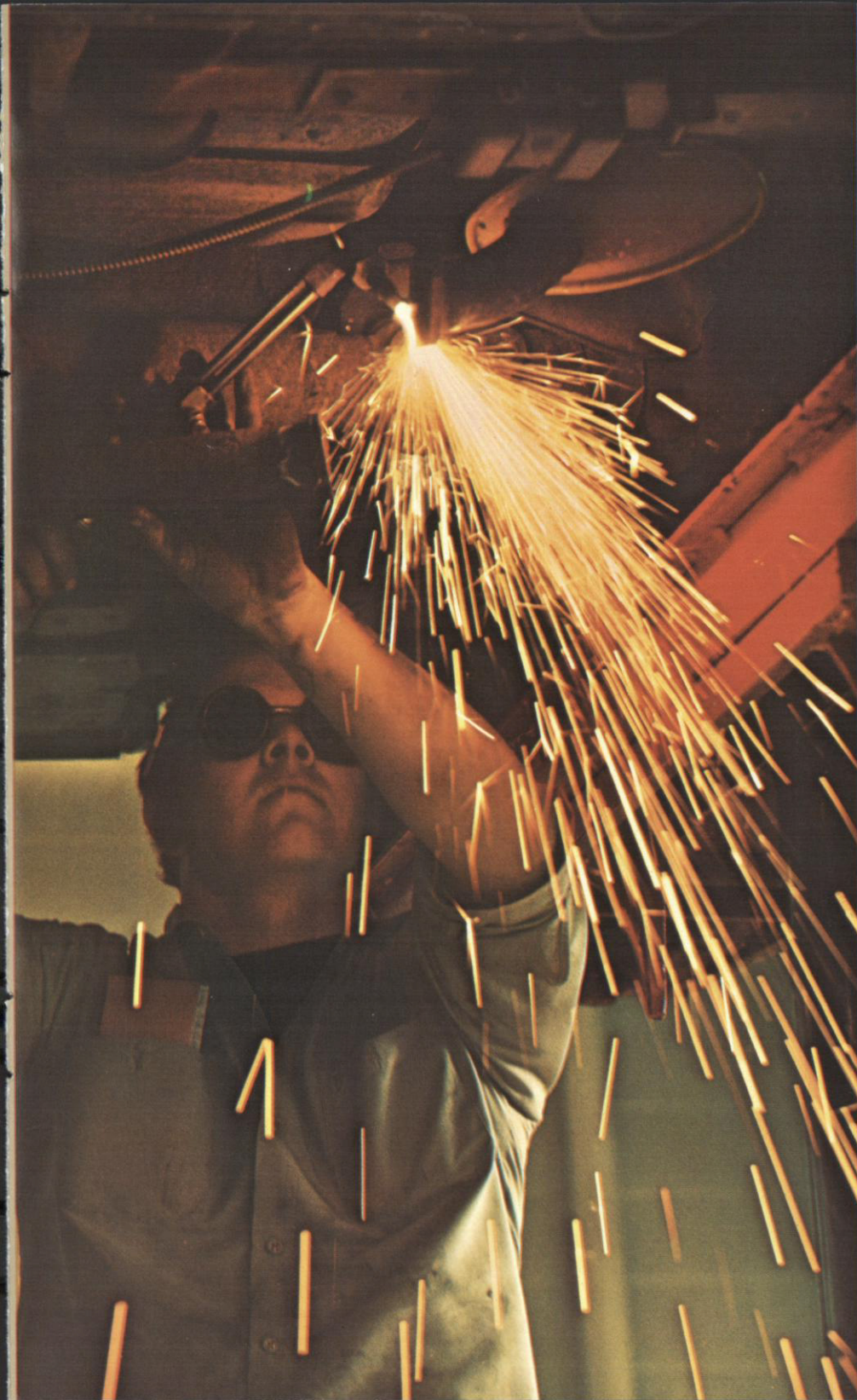
The majority of K mart automotive service departments show more than a 10 percent increase in volume each year.



K mart sound centers are among the most complete in the United States.

Qualified mechanics are on duty at all times in K mart automotive service areas.

Many sporting goods items are especially designed for K mart including snowmobile apparel.



1971 Financial Review

Sales Pass \$3 Billion Mark: Consolidated sales of \$3,100,216,000 for the 52 weeks ended January 26, 1972 were 21.2% above last year's record of \$2,558,712,000. Sales by division were:

	1971	1970	Percent Increase (Decrease)
K mart	\$2,557,212,000	\$2,014,358,000	27.0
Kresge	465,915,000	470,354,000	(.9)
Jupiter	77,089,000	74,000,000	4.2
	<u>\$3,100,216,000</u>	<u>\$2,558,712,000</u>	21.2

Net Income Exceeded \$96 Million in 1971: Net income rose to \$96,116,000, up 43.5% from last year's record \$66,994,000. Earnings per common and common equivalent share rose 37.6% to \$2.56 from \$1.86 last year. The rate of profit on sales was 3.10%, compared with the previous year's 2.62%.

The company's net income increased because of expanded and improved K mart operations and because general and administrative expenses did not increase proportionately as much as sales.

Earnings per common and common equivalent share of \$2.56 for the year ended January 26, 1972 were computed by dividing net income by the weighted average number of shares of common stock and common stock equivalents outstanding during the year. Common stock equivalents were less than 3% dilutive in the computation of \$1.86 for the year ended January 27, 1971; accordingly, such computation was based on the weighted average number of shares outstanding during that year.

In making the computation of earnings per common and common equivalent share for the year ended January 26, 1972, common shares at the beginning of the year were increased by the number of shares issuable on conversion of the 5% convertible debentures and net income was adjusted for interest expense and amortization of debenture expense net of related tax effect. The number of common shares was also increased by the number of shares issuable under the stock option and stock purchase incentive plans, less the number of shares which were assumed to have been purchased at average market prices with the proceeds of sales under the plans.

Earnings per common share assuming full dilution are not presented for the year ended January 26, 1972 because all dilutive securities are common stock equivalents and are therefore included in the per share computation which is presented. The fully diluted computation for the prior year resulted in dilution of less than 3%.

Subsidiary Company Profits Increased: Earnings of all subsidiary companies were improved compared with 1970, with K mart Enterprises, Inc. (operating all sporting goods and some automotive accessories departments in U. S. K marts) and the Canadian subsidiary showing results above expectations. As expected, Australian K marts were profitable after less than three years of operations.

Canadian operations are conducted through a wholly-owned Canadian subsidiary and Australian K marts are operated in a 51% owned Australian subsidiary. Assets of the foreign subsidiaries amounted to approximately 12% of the consolidated assets in 1971 and 11% in 1970, and net income of the foreign subsidiaries was 11% of consolidated net income for both years.

On December 30, 1971 the company purchased all of the common stock of Schiller Millinery Stores, Inc. which operates most U. S. K mart millinery departments and nine Detroit area millinery stores. The cost of this acquisition and another acquisition which became effective October 1, 1971 was not material in relation to consolidated assets and results of operations.

Dividends Were Increased: Quarterly dividends were raised to 12½¢ a share commencing with the June 12 payment, compared with 11¢ a share in effect during 1970—our seventh successive annual increase. Dividends declared amounted to \$18.2 million in 1971, compared with \$15.9 million in 1970.

Credit Sales Increased: Total credit sales for 1971 amounted to \$258,000,000, an increase of \$86,000,000 over 1970. The breakdown between the Kresge Thrifty Charge (KTC) sales and bank plan credit sales for the current and prior year and their percentage to total sales is as follows:

	1971		1970	
	Sales	% To Total Sales	Sales	% To Total Sales
KTC credit sales	\$154,000,000	5.0%	\$147,000,000	5.7%
Bankcard sales	104,000,000	3.3	25,000,000	1.0
	<u>\$258,000,000</u>	<u>8.3%</u>	<u>\$172,000,000</u>	<u>6.7%</u>

The first bank plans were established beginning in June 1970.

Service charges on Kresge Thrifty Charge accounts approximate the cost of administering the plan.

Year-end customer accounts receivable balances for 1971 and 1970 were 62.2% and 66.0% of KTC credit sales, respectively.

Working Capital Increased by \$43 Million: Working capital consists of current assets less current liabilities. The statements of changes in financial position appear on page 18.

Federal Income Taxes Were \$83 Million: The provisions for federal income taxes were at the effective rates of 46.4% and 48.5% in 1971 and 1970. The difference reflects the reinstatement of the investment credit of \$1,675,000 in 1971 compared with only \$170,000 in 1970 and changes in effective rates applicable to the company's wholly-owned U. S. subsidiaries. The current liability for U. S. and foreign income taxes includes \$11,149,000 at January 26, 1972 and \$10,089,000 at January 27, 1971 arising from the tax effects of timing differences related principally to profit on installment sales. The amounts shown on the balance sheets for deferred U. S. and foreign income taxes result from the difference between book and tax depreciation.

Stockholders' Equity Increased by \$92 Million: Stockholders' equity rose to \$548.5 million at January 26, 1972 from \$456.8 million at January 27, 1971 and amounted to \$15.00 and \$12.60 per share, respectively. Net income represented a return on stockholders' equity of 21.0% compared with 18.2% in 1970. Changes

in stockholders' equity, other than treasury stock and income retained for use in the business, for the fiscal years ended January 26, 1972 and January 27, 1971, were as follows:

	Common Stock (authorized 60,000,000 shares \$1.66 $\frac{2}{3}$ par value)		Capital in Excess of Par Value
	Shares	Amount	
Balance at January 31, 1970	34,713,059	\$57,855,000	\$20,871,000
Common stock sold under stock option and purchase plans	78,209	131,000	3,010,000
Conversion of 4 $\frac{1}{8}$ % debentures	1,456,409	2,427,000	32,618,000
Balance at January 27, 1971	36,247,677	60,413,000	56,499,000
Common stock sold under stock option and purchase plans	312,020	520,000	10,655,000
Excess of value received over cost of treasury shares issued in acquisition			2,312,000
Balance at January 26, 1972	<u>36,559,697</u>	<u>\$60,933,000</u>	<u>\$69,466,000</u>

The 27,718 shares of common stock which had been held in the company's treasury at a cost of \$338,000 were used to purchase the stock of another company as of October 1, 1971. There were no other transactions in treasury stock during the two-year period.

Ten million shares of no par value preferred stock with voting and cumulative dividend rights were authorized in May 1969 primarily for possible use in acquisitions but there are currently no plans for its use.

A Three-for-One Stock Split Is Planned: The Board of Directors intends to adopt, at its March 21, 1972 meeting, a proposal for a three-for-one stock split under which the present outstanding shares of \$1.66 $\frac{2}{3}$ par value will be converted to \$1.00 par and shareholders will be furnished two additional shares of \$1.00 par common for each \$1.66 $\frac{2}{3}$ par share held. This proposal is subject to approval by the stockholders at the annual meeting in June 1972 of a change in the authorized common stock to 250,000,000 shares of \$1.00 par value.

Long-Term Debt: Long-term debt as of January 26, 1972 compared with January 27, 1971 consisted of:

	January 26 1972	January 27 1971
5% convertible subordinated debentures	\$125,000,000	\$125,000,000
3 $\frac{1}{8}$ % and 4 $\frac{7}{8}$ % notes payable in varying amounts through December 16, 1983 (\$1,625,000 due within one year)	16,750,000	18,375,000
Foreign bank loans	8,560,000	2,811,000
Other	1,318,000	1,559,000
	<u>151,628,000</u>	<u>147,745,000</u>
Portion due within one year	1,779,000	1,880,000
	<u>\$149,849,000</u>	<u>\$145,865,000</u>

The debentures due in 1995 are convertible into common stock at \$53.50 a share. The indenture relating to the debentures provides that the company shall pay \$6,500,000 into a sinking fund before April 15 each year from 1981 to 1994. The debentures are subject to redemption through the sinking fund at 100% of principal amount, or at any time at the option of the company at prices declining from 105% to 100% of principal amount after April 15, 1990. At January 26, 1972, 2,336,449 shares of authorized common stock are reserved for conversion.

Under the long-term note agreements, \$95,000,000 of income retained at January 26, 1972 is available for payment of cash dividends.

Minimum Annual Rents Totaled \$120 Million: Minimum annual rents under 1,245 leases for stores occupied at January 26, 1972 aggregated \$120,658,000. These leases expire during 10-year periods as follows:

1982	\$ 13,520,000
1992	43,922,000
2002	61,563,000
2003-2035	1,653,000
	<u>\$120,658,000</u>

Certain leases provide for additional rent payments based on sales volume in excess of a specified base.

Most leases on K marts and certain leases on Kresge and Jupiter stores are gross leases under which the lessor pays property taxes, insurance and specified building and parking lot maintenance and repair costs.

Stock Option and Purchase Incentive Plans: The option and purchase plans were in effect before the Pay Board was established, and its regulations are not expected to affect the advantages which accrue to the company through ownership by employees of its common stock.

Information on stock purchase incentive and option plans is summarized below:

	Number of Shares	
	1971	1970
Stock purchase incentive plan—		
Shares available for purchase at beginning of year at 85% of market value	770,204	839,443
Shares purchased during the year through payroll deduction at \$34.85 and \$39.95 a share, respectively	(268,235)	(69,239)
Shares reserved but not purchased under the 1966 plan (terminated in 1971)	(501,969)	—
Shares available for purchase under the 1971 plan	<u>800,000</u>	<u>—</u>
Shares available for purchase at end of year	<u>800,000</u>	<u>770,204</u>

Under the stock purchase incentive plan approved by the stockholders in June 1971, employees of the company or of a subsidiary who have completed one

year of service are eligible to purchase, through June 1976, 800,000 shares of common stock by authorizing payroll deductions which shall not exceed 10% of the participant's compensation.

	Number of Shares	
	1971	1970
Stock option plan—		
Available for grant at beginning of year	141,360	186,760
Under option at beginning of year (\$38.32 to \$56.69 per share)	246,985	210,555
Options granted (\$38.32 to \$97.56 per share)	54,900	59,800
Options exercised (\$38.32 to \$56.69 per share)	43,785	8,970
Options cancelled (\$38.32 and \$41.88 per share)	2,680	14,400
Under option at end of year (\$38.32 to \$97.56 per share)	255,420	246,985
Options exercisable at end of year (\$38.32 to \$97.56 per share)	112,634	80,168
Available for grant at end of year	89,140	141,360

Under the qualified stock option plan approved by the stockholders in May 1969, options to purchase 400,000 shares of common stock may be granted to officers and key employees at 100% of the fair market value on the date of the grant. Options expire five years from the date of grant and are exercisable in annual installments, except that options granted to optionees over age 61 at the date of grant are exercisable in total at such date.

Retirement Income Plans Cost Over \$5 Million: The company and its subsidiaries have non-contributory retirement pension plans covering most employees. Eligibility is based on age and years of service. The total pension expense was \$5,363,000 and \$4,721,000 for the years ended January 26, 1972 and January 27, 1971, respectively. The company's policy is to fund pension costs accrued.

Company Expansion Continues

Kresge Operates 1,122 Stores: Kresge opened 75 K marts this year and now operates 486 K marts in the United States, Canada, Australia and Puerto Rico and 636 Kresge and Jupiter stores in the United States, Canada and Puerto Rico.

K marts are discount department stores with 75,000 to 95,000 square feet, Kresge stores are variety stores (called "dime stores" years ago) and Jupiter stores are small discount stores which were converted from Kresge operations.

75 K marts Were Opened:

	K mart	Kresge	Jupiter	Total
Stores in operation January 27, 1971	411	539	123	1,073
Stores opened	75	1	1	77
Closed permanently		(19)	(8)	(27)
Kresge stores converted to Jupiter		(1)	1	
Closed for fire restoration			(1)	(1)
Net change	75	(19)	(7)	49
Stores in operation January 26, 1972	486	520	116	1,122

Five Million Square Feet of Selling Area Was Added: Square feet of selling area now totals 39,615,000: (000 omitted)

	1971	1970	1969	1968	1967
K mart Stores					
United States	27,751	23,099	18,531	14,942	11,757
Canada	3,030	2,482	2,049	1,521	1,081
Australia	589	469	287	—	—
	31,370	26,050	20,867	16,463	12,838
Kresge Stores					
United States	6,442	6,682	6,910	7,143	7,366
Canada	926	945	959	1,032	1,045
	7,368	7,627	7,869	8,175	8,411
Jupiter Stores					
United States	789	822	795	835	857
Canada	88	94	90	24	24
	877	916	885	859	881
Grand Total	39,615	34,593	29,621	25,497	22,130

Square feet totals for prior years have been restated to conform with 1971 figures which reflect only stores in operation at year-end.

Distribution Center and Office Facilities Were Improved: Construction was completed on Holly Stores, Inc.'s 592,000 square-foot distribution center and administrative office in North Bergen, New Jersey. This facility began operations during the year and is considered to be the most modern and efficient ladies' ready-to-wear warehouse in the United States.

The one-million square-foot Lawrence, Kansas, distribution center commenced operations in November 1971. This is a fully automated and highly efficient facility which will be invaluable for keeping up with projected K mart growth.

Progress continued on the headquarters building in Troy, Michigan. The public relations department, credit offices and part of the research, personnel and data processing departments have moved and all other Detroit Office departments are scheduled to move at approximately midyear 1972.

Capital Expenditures Were More than \$82 Million: Additions to existing stores were made under a continuing program to modernize and renovate Kresge stores and some K marts opened in the early 1960's.

Changes in Fixed Assets Were:

	New Stores	Existing Stores, Distribution Centers and Office Buildings	Total
Additions:			
Buildings and leasehold improvements	\$ 2,740,000	\$38,561,000	\$41,301,000
Furniture and fixtures	32,474,000	22,644,000	55,118,000
Construction work in progress	2,648,000	(16,528,000)	(13,880,000)
	<u>\$37,862,000</u>	<u>\$44,677,000</u>	<u>82,539,000</u>
Retirements and disposals			(1,955,000)
Depreciation			(27,642,000)
Increase in net fixed assets			<u>\$52,942,000</u>

Purchase and construction commitments in connection with the company's expansion program amounted to approximately \$10,700,000 at January 26, 1972.

Management Recruiting and Training Programs Were Increased: Kresge and Jupiter store managers, who consistently demonstrated merchandising and leadership abilities, again provided the management personnel for the K marts opened in 1971. Many of these managers had served as Kresge or Jupiter district managers and most received K mart orientation, serving as K mart co-managers, prior to K mart management.

The company has established recruiting and training goals to meet the anticipated demand for management personnel during the 1970's. Over 2,700 men and women are presently involved in the four to six year training program to become Kresge and Jupiter store managers.

At the present time 62% of this group are college graduates, 16% have two or more years of college, and the remaining 22% have less than two years of college or are high school graduates.

Recruiting efforts and results throughout the country in 1971 were eminently successful. The parent company hired 800 college graduate trainees compared with 357 in 1970.

Statement of Accounting Policies

To assist the interested reader in understanding the accompanying financial statements, the more significant accounting policies followed by the company are explained below:

Basis of Consolidation: All majority owned subsidiary companies have been included in the consolidated financial statements. Other affiliated companies in which the company has more than a 20% interest are accounted for by use of the equity method. In consolidation, the assets, liabilities and operations of foreign subsidiaries were translated into U. S. dollars at appropriate rates of exchange. Translation gains included in income were not material.

Inventory: Inventories are valued at the lower of cost or market, using the retail method, on a first-in, first-out basis. Stock on hand more than a year is written off.

Property, Plant and Equipment: Land, buildings, leasehold improvements and equipment are carried at cost. Major replacements and refurbishings are charged to the property accounts while replacements, maintenance and repairs which do not improve or extend the life of the respective assets are expensed currently.

Depreciation: The company computes depreciation of fixed assets principally on the straight line method for financial statement purposes and on accelerated methods for income tax purposes. Most store properties are leased, and improvements are amortized over the term of the lease but not more than 25 years. Other annual rates used in computing depreciation for financial statement purposes are:

Buildings	2% to 8.86%
Fixtures and equipment—	
K marts	10%
Other	6%

Licensee Sales: The company's policy is to exclude sales of licensed departments from total sales.

Pre-Opening Costs: The company follows the practice of charging against net income costs incurred prior to opening a new retail unit.

Investment Credit: The company uses the "flow through" method of accounting for investment credit whereby income tax expense is reduced for the period in which expenditures create the tax benefit.

Opinion of Independent Accountants

15

To the Stockholders and Board of Directors
of S. S. Kresge Company

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and income retained for use in the business and changes in financial position present fairly the financial position of S. S. Kresge Company and its subsidiaries at January 26, 1972 and January 27, 1971, the results of their operations and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

211 West Fort Street
Detroit, Michigan
March 13, 1972

Price Waterhouse & Co.

Consolidated Statements of Income

Consolidated Statements of Income Retained for Use in the Business

	Fiscal Year Ended	
	January 26 1972	January 27 1971
Sales	\$3,100,216,000	\$2,558,712,000
Fees from licensed departments	39,437,000	36,443,000
Interest income	1,861,000	1,864,000
	<u>3,141,514,000</u>	<u>2,597,019,000</u>
Cost of merchandise sold (including buying and occupancy costs)	2,328,329,000	1,936,538,000
Selling, general and administrative expenses	622,201,000	518,961,000
Interest expense	10,640,000	10,545,000
Loss on disposals of fixed assets and cancellation of leases (net)	910,000	814,000
	<u>2,962,080,000</u>	<u>2,466,858,000</u>
Income before estimated income taxes	179,434,000	130,161,000
Estimated income taxes:		
U.S.	69,938,000	53,037,000
Foreign	10,095,000	7,675,000
Tax effects of timing differences	3,285,000	2,455,000
	<u>83,318,000</u>	<u>63,167,000</u>
Net income for the year	<u>\$ 96,116,000</u>	<u>\$ 66,994,000</u>
Earnings per common and common equivalent share	<u>\$2.56</u>	<u>\$1.86</u>

	Fiscal Year Ended	
	January 26 1972	January 27 1971
Income retained for use in the business at beginning of year	\$ 340,187,000	\$ 289,131,000
Net income for the year	96,116,000	66,994,000
Cash dividends declared—50¢ and 44¢, respectively	<u>(18,233,000)</u>	<u>(15,938,000)</u>
Income retained for use in the business at end of year	<u>\$ 418,070,000</u>	<u>\$ 340,187,000</u>

See 1971 Financial Review on pages 10 to 13 and Statement of Accounting Policies on page 15.

See 1971 Financial Review on pages 10 to 13 and Statement of Accounting Policies on page 15.

Consolidated Balance Sheets

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Assets	January 26 1972	January 27 1971	Liabilities	January 26 1972	January 27 1971
Current Assets:			Current Liabilities:		
Cash	\$ 54,926,000	\$ 52,368,000	Portion of long-term debt due within one year	\$ 1,779,000	\$ 1,880,000
Certificates of deposit	6,118,000	7,800,000	Notes payable to banks	29,625,000	21,670,000
Marketable securities, at cost approximating market	7,872,000	38,886,000	Accounts payable—trade	211,505,000	173,705,000
Customer accounts receivable, less allowance for possible losses of \$5,298,000 and \$5,522,000, respectively	90,460,000	91,465,000	Accrued taxes, other than U.S. and foreign income taxes	31,721,000	26,309,000
Other accounts receivable	11,000,000	9,698,000	Accrued payrolls and other liabilities	47,229,000	36,428,000
Merchandise inventories, at lower of cost (approximate first-in, first-out) or market	584,798,000	444,888,000	Dividends payable	4,570,000	3,984,000
Operating supplies and prepaid expenses	17,973,000	15,164,000	U.S. and foreign income taxes	43,054,000	35,622,000
Total current assets	773,147,000	660,269,000	Total current liabilities	369,483,000	299,598,000
Other Assets and Deferred Charges	11,535,000	7,634,000	Deferred U.S. and Foreign Income Taxes	26,565,000	24,003,000
Fixed Assets, at cost:			Long-Term Debt, less portion due within one year	149,849,000	145,865,000
Land	35,941,000	35,559,000	Minority Interest in Australian Subsidiary	1,582,000	
Buildings	99,208,000	65,115,000	Stockholders' Equity:		
Leasehold improvements	78,863,000	75,817,000	Common stock	60,933,000	60,413,000
Furniture and fixtures	296,562,000	248,648,000	Capital in excess of par value	69,466,000	56,499,000
Construction in progress	5,140,000	19,020,000	Income retained for use in the business	418,070,000	340,187,000
	515,714,000	444,159,000		548,469,000	457,099,000
Less—Depreciation and amortization	204,448,000	185,835,000	Less—27,718 shares in treasury at cost		338,000
	311,266,000	258,324,000		548,469,000	456,761,000
	<u>\$1,095,948,000</u>	<u>\$926,227,000</u>		<u>\$1,095,948,000</u>	<u>\$926,227,000</u>

See 1971 Financial Review on pages 10 to 13 and Statement of Accounting Policies on page 15.

Consolidated Statements of
Changes in Financial Position

	Fiscal Year Ended			Fiscal Year Ended	
	January 26 1972	January 27 1971		January 26 1972	January 27 1971
Financial Resources Were Provided by:			Analysis of Changes in Working Capital:		
Net income for the year	\$ 96,116,000	\$ 66,994,000	Increase (decrease) in current assets—		
Add (deduct) income charges (credits) not affecting working capital—			Cash and certificates of deposit	\$ 876,000	\$ 11,522,000
Depreciation and amortization	27,642,000	23,737,000	Marketable securities	(31,014,000)	32,989,000
Increase in deferred U.S. and foreign income taxes	2,562,000	1,475,000	Accounts receivable	297,000	781,000
Other	56,000	(1,405,000)	Merchandise inventories	139,910,000	45,302,000
Working capital provided by operations	126,376,000	90,801,000	Operating supplies and prepaid expenses	2,809,000	2,014,000
Sale of fixed assets	1,394,000	2,602,000		<u>112,878,000</u>	<u>92,608,000</u>
Sale of common stock under stock option and purchase plans	11,175,000	3,141,000	(Increase) decrease in current liabilities—		
Sale of 5% convertible debentures, less related expense of \$1,406,000		123,594,000	Long-term debt due within one year	101,000	(118,000)
Proceeds from long-term borrowings	8,560,000		Notes payable to banks	(7,955,000)	82,226,000
Other	3,997,000		Accounts payable—trade	(37,800,000)	(14,962,000)
	<u>151,502,000</u>	<u>220,138,000</u>	Accrued taxes, other than U.S. and foreign income taxes	(5,412,000)	(2,946,000)
Financial Resources Were Used for:			Accrued payrolls and other liabilities	(10,801,000)	(5,570,000)
Additions to fixed assets	82,539,000	58,720,000	Dividends payable	(586,000)	(515,000)
Cash dividends declared	18,233,000	15,938,000	U.S. and foreign income taxes	(7,432,000)	(7,987,000)
Reduction of notes and mortgages payable	4,576,000	1,880,000		<u>(69,885,000)</u>	<u>50,128,000</u>
Other	3,161,000	864,000			
	<u>108,509,000</u>	<u>77,402,000</u>			
Increase in Working Capital	<u>\$ 42,993,000</u>	<u>\$142,736,000</u>	Increase in Working Capital	<u>\$ 42,993,000</u>	<u>\$142,736,000</u>

See 1971 Financial Review on pages 10 to 13 and Statement of Accounting Policies on page 15.

10-Year Financial Review

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(Dollar amounts shown in thousands)	1971	1970	1969	1968	1967	1966	1965	1964	1963	1962
Sales	\$3,100,216	\$2,558,712	\$2,185,298	\$1,731,533	\$1,385,694	\$1,090,181	\$851,443	\$688,776	\$543,671	\$483,013
Net income	\$ 96,116	\$ 66,994	\$ 54,089	\$ 47,611	\$ 34,915	\$ 28,609	\$ 22,154	\$ 17,374	\$ 11,089	\$ 9,053
% to Sales	3.10%	2.62%	2.48%	2.75%	2.52%	2.62%	2.60%	2.52%	2.04%	1.87%
Earnings Per Share:										
Common and Common Equivalent	\$ 2.56	\$ 1.86	\$ 1.57	\$ 1.39	\$ 1.03	\$.85	\$.67	\$.53	\$.34	\$.27
Assuming Full Dilution	2.56	1.83	1.52	1.35	1.02					
Cash Dividends Declared	\$ 18,233	\$ 15,938	\$ 13,841	\$ 11,656	\$ 10,188	\$ 8,702	\$ 7,761	\$ 6,602	\$ 6,607	\$ 8,273
Per Share	.50	.44	.40	.34	.30	.26	.23	.20	.20	.25
K mart, Kresge and Jupiter Stores	1,122	1,073	1,022	982	943	915	895	885	854	821
Inventories of Merchandise	\$ 584,798	\$ 444,888	\$ 399,586	\$ 304,236	\$ 223,933	\$ 166,084	\$136,187	\$108,266	\$ 90,796	\$ 81,172
% to Sales	18.86%	17.39%	18.29%	17.57%	16.16%	15.23%	15.99%	15.72%	16.70%	16.81%
Net Working Capital	\$ 403,664	\$ 360,671	\$ 217,935	\$ 198,521	\$ 171,360	\$ 123,798	\$110,739	\$ 93,362	\$ 83,969	\$ 63,595
% to Sales	13.02%	14.10%	9.97%	11.47%	12.37%	11.36%	13.01%	13.55%	15.44%	13.17%
Net Worth	\$ 548,469	\$ 456,761	\$ 367,519	\$ 319,450	\$ 275,632	\$ 251,803	\$229,597	\$212,419	\$202,544	\$197,996
Per Share	15.00	12.60	10.67	9.27	8.10	7.46	6.87	6.42	6.12	5.48
Long-Term Debt	\$ 149,849	\$ 145,865	\$ 57,753	\$ 61,190	\$ 63,476	\$ 26,254	\$ 27,869	\$ 29,407	\$ 31,182	\$ 16,983
Fixed Asset Additions less Retirements	\$ 80,584	\$ 56,118	\$ 45,693	\$ 33,544	\$ 26,866	\$ 22,720	\$ 13,188	\$ 14,724	\$ 12,638	\$ 11,739

Per share calculations give effect to 1968 three for one and 1966 two for one stock splits.

S. S. Kresge Company A Michigan Corporation

Executive Offices

2727 Second Avenue, Detroit, Michigan 48232

Subsidiaries

S. S. Kresge Company Limited, Toronto, Ontario, Canada
Holly Stores, Inc., North Bergen, New Jersey
K mart (Australia) Limited, Melbourne, Victoria, Australia
K mart Enterprises, Inc., Royal Oak, Michigan

Directors

Arnold H. Bachner	Robert E. Dewar	Robert W. Purcell
William H. Baldwin	Stanley S. Kresge	George Russell
Henry T. Bodman	Rolland Lawson	Walter H. Teninga
Morgan Collins	Albert W. Ley	Ervin E. Wardlow
Harry B. Cunningham	Paul W. McCracken	

Officers

Harry B. Cunningham, *Chairman of the Board and Chief Executive Officer*
Robert E. Dewar, *President and Chief Administrative Officer*
Ervin E. Wardlow, *Executive Vice President, Merchandising*
Robert H. Griffin, *Executive Vice President, Store Management*
Walter H. Teninga, *Executive Vice President, Corporate Development*
Albert W. Ley, *Vice President, International Operations*
Chester E. Boyd, *General Vice President*
Roger E. Davis, *Vice President-General Counsel and Secretary*
John C. Cook, *Vice President, Real Estate*
Henry G. McIntosh, *Vice President, Management Services*
Richard H. Black, *Vice President-Treasurer*
Dale A. Feet, *General Controller*
Richard H. Falck, *Vice President, Sales*
William R. Marshall, *Vice President, Merchandising Subsidiaries and K mart Licensees*
Lee W. Zane, *Vice President, Personnel and Employee Relations*
Harold A. Siegel, *Vice President, Food Operations*
Harvey E. Chapman, *Vice President, Transportation and Distribution*
Kenneth L. Dunkel, *Vice President, Merchandise Systems and Distribution Center Operations*
Russell A. Hansen, *Vice President and General Manager, Kresge and Jupiter Stores*
Edward C. Andrews, *Vice President, Southern Region*
Bernard M. Fauber, *Vice President, Western Region*
Grant W. Morck, *Vice President, Central Region*
William A. Saum, *Vice President, Eastern Region*
Robert J. Young, *Vice President, Midwestern Region*

Executive Committee

Harry B. Cunningham, *Chairman*
William H. Baldwin
Robert E. Dewar
Walter H. Teninga
Ervin E. Wardlow

Finance Committee

Harry B. Cunningham, *Chairman*
William H. Baldwin
Henry T. Bodman
Morgan Collins
Robert E. Dewar
George Russell

